DOCUMENT RESUME

ED 241 818 CE 800 122

TITLE	Ways to Save Your Money. The CIRcular: Consumer Information Report 2.
INSTITUTION	Bank of America NT & SA, San Francisco, CA.
PUB DATE	Nov 83
NOTE	5p.; For related documents, see CE 800 121-133.
AVAILABLE FROM	Bank of America, Dept. 3401, Box 37128, San Francisco, CA 94137 (first set free, $0.10 per copy thereafter, 10 copies $1.00, 100 copies $7.00).
PUB TYPE	Guides - Non-Classroom Use (055)
EDRS PRICE	MF01 Plus Postage. PC Not Available from EDRS.
DESCRIPTORS	*Banking; *Consumer Education; Guidelines; Investment; *Money Management; Pamphlets; Planning
IDENTIFIERS	PF Project; *Savings Accounts

ABSTRACT

This report explains savings accounts and low-deposit investments in order to help consumers determine which accounts are right for them. It is divided into the following four sections (topics covered are listed in parentheses): (1) the savings program (setting savings goals, saving regularly, choosing a savings account, interest, the savings contract, and places to save); (2) types of savings accounts (regular savings accounts, time deposit accounts, money market deposit accounts, "super NOW" accounts, and United States savings bonds); (3) investments (mutual funds and money market securities, the latter including United States Treasury issues, federal agency issues, municipal bonds, and corporate bonds); and (4) special purpose accounts (Christmas clubs, custodial and informal trust accounts, matching fund investment plans, Individual Retirement Accounts (IRAs), and Keogh plans). Information in this report is current at the time of printing, November 1983, but is subject to change. (DC)

****
* Reproductions supplied by EDRS are the best that can be made *
* from the original document. *
****

The CIRcular
Consumer Information Report 2

"PERMISSION TO REPRODUCE THIS MATERIAL IN MICROFICHE ONLY HAS BEEN GRANTED BY
Albert J. Dytch
TO THE EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)."

U.S. DEPARTMENT OF EDUCATION
NATIONAL INSTITUTE OF EDUCATION
EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)
This document has been reproduced as received from the person or organization originating it.
✓ Minor changes have been made to improve reproduction quality.
• Points of view or opinions stated in this document do not necessarily represent official NIE position or policy.

ED241818
CE 800 122

Ways to Save Your Money

Today, you can choose from more ways and places to save than ever before. This report describes the savings and low-deposit investments available and can help you determine which accounts are right for you.

Your Savings Program

In today's uncertain economic environment, it's more important than ever to have a carefully thought-out savings program. By accumulating a sum of money, you can help establish financial security, and you can take advantage of a broader range of choices for spending and investing.

Before you start to plan your savings program, however, you'll need to become familiar with the various aspects of saving and the variety of savings options available. And, to select the account or combination of accounts that best suits your needs, you should define your savings goals.

SET SAVINGS GOALS You're more likely to save if you're working toward a goal. Your goal might be to save for a vacation or for upcoming expenses such as taxes or insurance. Or, you may want to accumulate enough for a down payment on a house or establish a fund for retirement.

In addition to other savings goals, a good savings program includes funds set aside and readily available for emergencies. Generally, two to six months' take-home pay is a good range for an emergency fund. However, you should determine your own need by considering your current personal or family situation and the state of your finances, including debts.

Keep in mind that you may have emergency resources other than your savings. For example, you may be able to obtain emergency funds through insurance, Social Security, or employee benefits. You also may have assets, such as stocks or bonds, that you could readily convert to cash.

SAVE REGULARLY You can reach your savings goal—one payday at a time—by developing a savings habit. One way is to budget for savings each month, just as you would for rent, insurance, or loan payments. Decide to save a percentage of your income—2%, 5%, 10%, or whatever you can—and stick to your decision.

If your employer offers a payroll deduction plan, you can arrange to have money from your paycheck automatically deposited on a regular basis to a savings account at your bank or other financial institution.

If you're strapped for funds to save, consider

increasing your tax exemptions if your withholdings are higher than they need be. You can put the extra money in a savings or other type of account and earn interest on it.

CHOOSING A SAVINGS ACCOUNT To choose a savings account that's right for you, you'll first need to think realistically about yourself—your financial situation, your goals, and the period of time in which you want to reach them. Then, find the financial institution and savings account that are best suited to your particular needs. Keep four major considerations in mind.

1. Return The amount your savings can earn in interest.

2. Security The safety of your savings. The more secure your savings account is, the less your risk of loss from bankruptcy of an uninsured financial institution and the less likelihood that your account will fail to pay interest or return your principal.

3. Liquidity The speed with which you can obtain your money without financial penalty.

4. Convenience The ease with which you can manage your savings plan. Take into account the location of the financial institution where you save and the kind and quality of services offered.

Because no single type of savings account is likely to measure up to all your financial requirements, you might use a combination of savings methods. For instance, you could invest a portion of your savings in a time deposit account and keep the rest in a regular savings account. The time deposit account would probably bring a higher return, while the savings account would offer greater liquidity.

INTEREST Interest is the amount you receive in exchange for the use of your money. To compare savings plans, you'll need to understand the following.

Annual Interest Rate The amount of interest that you receive over a one-year period is expressed as a percentage called the annual interest rate. This rate may be fixed; or, it may increase or decrease at specified intervals (such as daily or weekly), depending on market conditions.

Annual Yield The annual interest rate is only one of several factors that determine how much you'll earn on the funds in your savings account. A different percentage figure—*annual yield*—is usually a more accurate expression of your interest earnings. Annual yield is calculated on the assumption that deposits and interest stay in the account for one full year. Also reflected in the annual yield is the method of calculating interest.

With the *simple interest* method, interest is calculated on your balance—your deposits plus any interest that's been paid to your account. If your account pays a 5½% simple annual interest rate, your annual yield is also 5½%. That means a balance of $100 earning 5½% simple annual interest would pay $5.50 in interest in the course of one full year.

With the *compound interest* method, interest is calculated on your balance plus any interest you've earned that has not yet been paid to your account. In other words, you earn interest on your interest.

Interest compounding increases your interest earnings—even though the annual interest rate remains the same. If your account pays a 5½% annual interest rate, your annual yield is 5.65%. A balance of $100 earning 5½% interest, compounded daily, would pay $5.65 in interest during one year.

The more frequently interest is compounded, the greater the yield on your savings account.

Balance Computation Each time you make a deposit or a withdrawal, it affects your interest earnings. With the most common method of balance computation—"day

COPYRIGHT © BANK OF AMERICA NT&SA 1979, 1981, 1983

of deposit to day of withdrawal"—you earn interest on the exact amount in your account each day.

However, financial institutions can use other methods of balance computation that are not as favorable for you. Make sure you understand how balance is calculated on the account you have in mind.

Other Points to Consider The amount of interest earnings you actually receive can be affected in several ways. Many accounts do not *credit* (pay) interest daily. Some pay interest at the end of each calendar month or quarter. Others pay interest at the end of a specified period of time called the term or maturity period.

Another consideration is the daily interest rate. Some institutions calculate daily interest at 1/360 the annual interest rate, others at 1/365. You should also find out what maintenance charges and service fees are involved.

THE SAVINGS CONTRACT The signature card you sign when you open a savings account is a legal contract. You may also receive, as part of the contract, other printed material containing the terms and conditions that apply to your account. You should be given this material when you open the account, but ask for it earlier—when you're shopping for a savings account.

PLACES TO SAVE Following are the major types of financial institutions that offer savings accounts.

Banks You can receive a wide range of financial services at a bank. These include: savings and time deposit accounts; regular and interest-bearing checking accounts; money market deposit accounts; Individual Retirement Accounts (IRAs); consumer, business, and real estate loans; and trust, investment, international, and business services. Deposits in member banks are insured for up to $100,000 by the Federal Deposit Insurance Corporation (FDIC).

Savings and Loan Associations (S&Ls) These institutions provide much of the money used to finance homes in the United States. Other services S&Ls can offer include savings and time deposit accounts, interest-bearing checking accounts, money market deposit accounts, IRAs, consumer loans, and trust services. Deposits in member associations are insured for up to $100,000 by the Federal Savings and Loan Insurance Corporation (FSLIC).

Credit Unions These are nonprofit savings and lending organizations that provide services to members. (Members must have a common bond through employment at the same firm, residence in the same community, or participation in the same group.) Credit unions can offer a variety of services, including savings and time deposit accounts, interest-bearing checking accounts, money market deposit accounts, IRAs, consumer and real estate loans, and certain investment services. Deposits in federal- and state-chartered credit unions are insured for up to $100 000 through the National Credit Union Administration.

Industrial Loan Companies These are a type of finance company that offers savings accounts. Besides making consumer and real estate loans, these companies issue investment certificates similar to passbook savings accounts. Certificates are protected for up to $50,000 through the Thrift Guarantee Corporation.

Other Financial Institutions Brokerage houses, mutual fund companies, and other institutions may offer a wide variety of financial services including such savings plans as time deposits and money market deposit accounts. However, the terms and the security of their savings accounts may differ substantially from similar accounts offered at the more traditional places to save.

Types of Savings Accounts

Savings accounts are a basic component of most savings programs. They provide a high degree of convenience and security and, usually, a predictable rate of return. You may choose from many types of savings accounts, from low-yielding regular savings accounts to higher-yielding time deposit and money market accounts. Each type has its own rules on deposits, withdrawals, payment of interest, and charges.

REGULAR SAVINGS ACCOUNTS A good way to start a savings program is with a regular savings account because of the low opening deposit requirement, but the annual interest rate is limited by law to 5½%. You can use this account to accumulate funds to meet the deposit requirements of accounts that pay higher interest. Regular savings accounts can be of value, too, as a place for emergency and short-term savings since there's no penalty for early withdrawal.

Sometimes called a passbook account, a regular savings account is the most basic and flexible type of savings account available. You may be required to deposit a certain amount to open an account, but you can make deposits to your account in virtually any amount at any time.

Generally, you can withdraw money from the account at any time. However, some institutions may limit the number of withdrawals you can make during a given period without charge. Others also may impose a monthly service charge if your balance falls below a certain amount. And, you may be charged a fee if you close your account before a specified period.

TIME DEPOSITS With a time deposit account, you agree to leave your money on deposit until the end of a specified period called the term or maturity period. In exchange, you receive an interest rate that is usually higher than the rate on regular savings accounts.

A time deposit account is a good place to put your money if you don't need immediate access to it. However, time deposit accounts are available for a wide range of terms, so you can choose a term that best fits your financial needs.

Within federal and state guidelines, financial institutions are permitted to offer time deposit accounts with different deposit requirements, terms, interest rates, and withdrawal restrictions.

Initial Deposits The minimum deposit required to open a time deposit account varies widely—from as low as $100 to as high as $2,500 or more.

Terms These range from 7 days to 10 years. With most time deposit accounts, the term begins on the day of deposit. However, with one type of time deposit account, called a passbook time deposit, terms consist of calendar quarters. If you deposit funds on any day other than the first business day of the calendar quarter, the term for that deposit won't begin until the first business day of the next quarter.

Interest Rates The term and the minimum deposit determine the annual interest rate. Rates may be fixed for the maturity period, or they may vary daily or weekly. Variable rates are usually based on the auction rates for U.S. Treasury Bills.

Additional Deposits You cannot make additional deposits to many of these accounts. Instead, you must open a new account with its own maturity period. Usually, your account stops earning interest on the maturity date.

Some accounts allow you to add funds. However, a minimum may be required, and you may have to make the deposit during a specified period of time at the end of the term. If you're allowed to add funds, the maturity date for the entire account may be extended for the same length of time as the original term. Or, each new deposit may have its own maturity period.

With many accounts, after the maturity date your funds are reinvested unless you withdraw them within a certain number of days. During this time, you also may be allowed to withdraw part of your funds. Generally, the funds left on deposit will be reinvested on the day of the withdrawal.

Early Withdrawal Penalties If you make a withdrawal from a time deposit account before the end of the maturity period, federal law requires a substantial interest penalty on the amount withdrawn. In some cases, the penalty may exceed the interest you have earned and include some of the principal. Financial institutions can impose additional penalties as well. Make sure you understand the penalties involved.

MONEY MARKET DEPOSIT ACCOUNTS If you can meet the $2,500 minimum deposit requirement, you may want to open a money market deposit account because it combines high yield, liquidity, and the safety of federal insurance.

This account is like a regular savings account in that you can withdraw your money at any time without penalty. It's different from a regular savings account in that it pays a variable rate of interest, comparable to the *money market rates*—the current interest rates paid on short-term private and government securities. However, if your average daily balance falls below $2,500, the interest rate usually drops to 5¼% annual interest.

Each statement period, you're allowed to make a total of six transfers, including three checking transactions, to another person, another organization, or accounts you have at another financial institution.

SUPER NOW ACCOUNTS If you regularly maintain a checking balance of $2,500, you may want to consider the Super NOW account. This account pays a variable rate of interest that is usually slightly lower than the rate on a money market deposit account, at the same institution. But, with a Super NOW you may write as many checks as you wish.

Until recently, the types of interest-bearing checking plans were limited to the regular NOW (negotiable order of withdrawal) accounts and credit union share draft accounts. A negotiable order of withdrawal and a share draft function like checks except that you write them against a savings account instead of a checking account.

NOW accounts usually pay 5¼% fixed interest; most credit union share draft accounts yield 5½% to 6%. With the Super NOW accounts offered by most banks and S&Ls, you earn a higher rate as long as you maintain an average daily balance of $2,500 or more.

As with most interest-bearing checking accounts, you benefit from a Super NOW if you keep at least the minimum balance and write only a few checks. If you write a lot of checks, the fees for such transactions could offset the interest you earn. Shop carefully for this and other interest-bearing checking accounts; be sure you understand the terms and conditions involved.

U.S. SAVINGS BONDS These are among the most convenient securities to purchase and redeem. They're extremely safe, and your interest earnings aren't subject to state or local income tax.

The federal government currently offers two types of savings bonds: Series EE and Series HH. Series E and Series H bonds are no longer available, but if you own any of them now, they'll continue to earn interest until their final maturity.

Series EE These bonds are available in denominations of $50 to $10,000. However, they're sold *at a discount*—at less than face value. You purchase an EE bond for 50% of the face value printed on the bond and redeem it for full face value at maturity. The maturity period is determined by how long it takes to accumulate enough interest to double the issue value of the bond.

Series EE bonds you purchase now will earn interest at a fixed rate that increases on a graduated scale for the first five years, to a maximum of 7½% compound annual interest. Bonds you hold at least five years pay a variable rate tied to money market rates. When you redeem the bonds, you receive an average for the term; you're guaranteed a minimum of 7½%, compounded annually. Bonds you bought before November 1982 must be held at least five years after that date to qualify for the variable rate.

Interest is paid to you when you redeem your bonds; you can do so any time after six months from the issue date. (For the current interest rate and approximate maturity period, contact your financial institution.)

You can buy Series EE bonds at most financial institutions or through a payroll deduction plan if your employer offers one.

Series HH These bonds are no longer available for purchase; the only way to get a new HH bond is in exchange for an E or EE bond. HH bonds are issued in denominations of $500 to $10,000 and earn a fixed interest rate. You obtain them at face value, and every six months the U.S. Treasury sends you a check for your interest earnings.

Although the maturity period for HH bonds is ten years, you may redeem them any time after six months from the issue date. However, if you obtained an HH bond for cash and redeem it before five years have passed, you'll receive less than face value.

Most financial institutions that issue EE bonds have the forms you need to exchange Es and EEs for HHs. You also can trade for HH bonds at a Federal Reserve Bank or, by mail, through the Bureau of the Public Debt, U.S. Treasury Department, Washington, DC 20226.

Investments

The line between saving and investing isn't always clear. Generally, when you invest, you seek a higher rate of return than when you save; in exchange, you usually must sacrifice some liquidity or security. There are, however, ways to invest with a minimum risk and with a relatively small initial deposit.

MONEY MARKET SECURITIES When you invest in money market securities, you make a short-term loan to one of a broad range of borrowers—the U.S. Treasury, a federal agency, a state or local government, or a corporation. You can purchase securities through a bank or broker. Normally, you'll pay a fee on transactions of less than $100,000. Money market securities may be held until maturity or sold to another investor. Although they're easy to sell on short notice, the price you receive can vary each week.

U.S. Treasury Issues These are considered to be among the safest investments you can make because they're backed by the U.S. government. The Treasury Department issues three types of securities: notes, bonds, and bills.

Treasury notes have maturities of 2 to 10 years; bonds have maturities of 10 to 30 years. These securities pay interest semiannually and are redeemed at maturity. Usually, notes with maturities of less than 4 years are issued in denominations of $5,000. Treasury notes with longer maturities and Treasury bonds are available in denominations of $1,000 or more.

Treasury bills, or T-bills, have maturities of 13, 26, or 52 weeks. They're sold at a discount and are redeemed for face value at maturity. The minimum denomination is $10,000. You can buy T-bills through a commercial bank or a broker or directly from a Federal Reserve Bank. The bills are held for you in a safekeeping account rather than issued in paper form. If you purchase T-bills from the Federal Reserve Bank, there's no commission or safekeeping fee. However, commercial banks and brokers may charge a service fee, safekeeping fee, or both.

Federal Agency Issues These securities represent the debt of various federal agencies that administer selected lending programs of the U.S. government.

Agency securities offer the advantage of a generally higher return than you can receive on U.S. Treasury issues. Minimum denominations vary with each agency. Some are as low as $1,000, but a $5,000 minimum is typical. Maturities range from a few months to 30 years. Most agency securities must be held in safekeeping for you by a bank or broker; you'll be charged for this service.

Municipal Bonds These are the debt obligations of state or local governments or state agencies. Typically, municipal bonds are issued in denominations of $5,000. However, to offset the risk involved with these bonds, investment counselors generally recommend buying at least three issued by different agencies.

Interest earned on municipal bonds is exempt from federal income tax and, in most cases, from state and local taxes in the state where the bonds are issued. Depending on your tax bracket, these tax exemptions can increase your return by a sizable amount.

When buying bonds, consider the issuer's creditworthiness. Several independent services provide credit ratings using a standardized system. Reports by two such services, Standard & Poor's and Moody's, are available at most public libraries.

Bonds with a good credit rating generally will provide you with greater investment security, but those with lower ratings frequently offer higher interest rates as compensation for greater risk.

Corporate Bonds These represent the borrowings of corporations. Minimum denominations vary with each company but typically start at $1,000. Some bonds are backed only by the company's promise to pay; others are backed by specific assets. In the latter case, if the company can't meet the

interest payments, the property could be sold to repay bond holders. As with municipal bonds, you should consider the issuer's credit rating before you buy.

Corporate bonds usually pay a higher interest rate than U.S. government bonds or tax-free municipals with the same credit rating. However, interest earnings are taxable.

MUTUAL FUNDS In recent years, mutual funds have become an increasingly popular investment. With a minimum of $500 to $1,000, you can generally participate in a broad range of investments.

When you invest in a mutual fund, you buy shares in a portfolio of securities managed by professionals. The interest rate you receive depends on how much the fund's securities are earning. Some funds specialize in only one kind of security or industry; most offer a variety and, therefore, a means to minimize risk. If your fund belongs to a "family of funds"—an investment group that offers several types of funds—you can switch money from one fund to another to take advantage of changes in market conditions.

One of the most popular types of funds is the money market mutual fund. It may invest in a variety of money market securities or in only one type, such as U.S. Treasury Bills. As with a money market deposit account, you can withdraw your money at any time without penalty. However, you can write an unlimited number of checks, usually for a specified minimum amount such as $250 or more, and the minimum deposit can be as little as $100 or less. Keep in mind, though, that your money is not protected by federal insurance.

Mutual funds are required by law to state their investment policies; you can use these statements to select funds that match your investment goals. You can buy fund shares through brokers or directly from mutual fund corporations.

Special Purpose Accounts

Many financial institutions offer accounts tailored to fit certain goals such as meeting holiday expenses, administering funds for another person, or generating retirement income.

CHRISTMAS CLUBS The purpose of these accounts, whether they're called Christmas Clubs or some other name, is to help you save for year-end or holiday expenses. With this type of account, you agree to make deposits in equal amounts at regular intervals over a year's time. Generally, you cannot withdraw your money until a year has passed. Some accounts pay no interest. Others pay the same rate as a regular savings account.

Under most plans, you either set the total savings goal for the year or the amount of your regular deposit. Depending on the plan, you may have deposits transferred automatically from your checking or savings account. Or, as a reminder, you may be given a book of dated coupons to send in with your deposits.

CUSTODIAL AND INFORMAL TRUST ACCOUNTS These are designed to benefit another person. They're available in the form of savings and time deposit accounts, money market deposit accounts, and regular and interest-bearing checking accounts.

As an adult, you can open a custodial account for a minor. The account is transferred to the child when he or she reaches the age of 18. The child is considered the legal owner of the funds, and there are restrictions regarding deposits and withdrawals you can make. This type of account usually is opened under the advice of an attorney.

With an informal trust account, you're considered the legal owner of the deposited funds. After your death, funds in the account automatically belong to the person you named as beneficiary.

Alternatively, you can sign a pay-on-death agreement designating a beneficiary. As with an informal trust account, the funds are automatically released to your beneficiary when you die.

MATCHING FUND INVESTMENT PLAN Your employer may offer a matching fund investment plan, often called a thrift plan. In general, you're offered a choice of investments ranging from the company's stock to a fund that invests in a variety of other stocks. After you make a choice, you contribute a percentage of your gross pay each month, usually between 1% and 6%. Each dollar you put in is matched by your employer—typically with 50 cents or another dollar—up to a certain limit.

If you leave the firm, you get your money back plus any earned interest. You also may be entitled to your employer's contributions; plans vary in how long you must be with the company or participate in the plan for this to happen. If it's a qualified employer retirement plan, no tax is due on your employer's contributions or on earnings on all contributions until you receive the funds.

INDIVIDUAL RETIREMENT ACCOUNTS (IRAs) Even if you're covered by a qualified employer retirement plan, you can open an IRA. You can contribute up to $2,000 or 100% of your annual earned income, whichever is less. If you're married and your spouse does not work, you can contribute a combined total of $2,250 to IRAs on your and your spouse's behalf. (If your spouse works, each of you may contribute $2,000 or 100% of earned income.) You can deduct these amounts on your federal income tax return. You may also be able to deduct a portion of your contribution on your California income tax return. (Contact the State Franchise Tax Board for state tax requirements.)

Earnings on your IRA are not subject to federal or state income tax until you withdraw them. However, with certain exceptions, you must pay interest and tax penalties if you withdraw funds from your IRA before you reach age 59½.

If you own your own business or are self-employed, you can also set up a Simplified Employee Pension (SEP) plan for yourself and your employees. Under a SEP, you may contribute 15% of your annual earnings or $15,000, whichever is less, to an IRA. In general, you must contribute the same percentage of your employee's earnings to IRAs on their behalf.

KEOGH PLAN If you're self-employed, you can generally establish your own pension program through a Keogh plan. Each year you can set aside 15% of your annual earned income or $15,000, whichever is less. For the 1984 tax year, the limit is 25% of your annual earned income or $30,000, whichever is less.

Depending on the amount you contribute to your Keogh plan, you may be able to deduct all or part of it on your federal income tax return. You also can deduct a limited amount on your California income tax return. (Contact the State Franchise Tax Board for state tax requirements.)

No tax is due until you withdraw funds from the plan. However, with certain exceptions, you must pay interest and tax penalties if you withdraw funds before you reach age 59½.

When you begin a Keogh plan for yourself, you also must include employees who meet certain requirements. Generally, you cannot establish both a Keogh and SEP plan. Because setting up a Keogh or a SEP plan can be complex, you should consult your attorney or tax adviser. (For more information about retirement plans, see Report #6 in this series, *Planning for Retirement Income.)*

Making Your Program Work

As your financial situation and goals change, you'll need to make adjustments to your savings and investment program. When you're just starting out, you may need the liquidity and relatively high yield of a money market account to help you furnish a home or provide for a growing family. When you're older, you can probably start to put money into a long-term retirement account and feel comfortable about making some low-risk investments.

Whatever your savings strategy, you'll see the reward of your efforts as you reach each of your savings goals.

Information in this report is current at the time of printing, November 1983, but is subject to change.

Prepared by Bank of America, Box 37128, San Francisco, California 94137

BANK OF AMERICA NT&SA • MEMBER FDIC

AD-252 (11 83)